

Legislative Notice

No. 43

June 12, 2002

S. 2600 – Terrorism Reinsurance Bill

Calendar No. 410

Introduced June 7, 2002, read the second time, and placed on the Senate Calendar June 10, 2002, under Rule 14. No report.

NOTEWORTHY

- S. 2600, sponsored by Senators Dodd, Reid, Sarbanes, and Schumer, was introduced June 7, 2002, and placed directly on the Calendar on June 10. The bill is similar to the Democrat approach offered to the Senate prior to Christmas last year.
- The bill would provide a temporary federal backstop to existing and future insurance policies covering terrorist attacks. The bill would make taxpayers explicitly liable for 90 percent of losses exceeding \$10 billion that are the result of a terrorist attack.
- Under S. 2600, taxpayers could be liable for 80 percent of losses significantly below \$10 billion when those losses exceed caps applied to individual insurance companies.
- Another bill, S. 1748, sponsored by Senators Gramm, Allard, Bennett, Bunning, and Enzi, was placed directly on the Calendar December 3, 2001. That bill represents the bipartisan agreement among the Bush Administration, Senators Gramm, Enzi, *et al.*, and Democrat Senators Dodd and Sarbanes of November 1, 2001. That bill was derailed by Majority Leader Daschle over its liability reforms.
- The House passed H.R. 3210, the Terrorism Risk Protection Act, on November 29 by a vote of 227-193. That bill is also on the Senate Calendar. H.R. 3210 would insure losses above \$100 million. Unlike the Senate bill, the House bill would (a) recapture taxpayer losses through assessments on insurance companies and (b) include significant liability reforms. The Administration supported passage of H.R. 3210 with reservations.
- A recent letter from four high officials in the Administration outlined concerns regarding the lack of liability reform in S. 2600. The letter states, “We would recommend that the President not sign any legislation that leaves the American economy and victims of terrorist acts subject to predatory lawsuits and punitive damages. (See “Administration Position,” p. 5.)

BACKGROUND

Following September 11, 2001, Congress has taken several steps designed to assist those harmed by the terror attacks, prepare for any subsequent attack, and prevent further attack from occurring. These steps include passing the Use of Force resolution, the Air Transportation Safety and Stabilization Act, and the Bioterrorism Preparedness Act.

A related effort involved providing a federal backstop to insurance policies covering acts of terrorism. By most accounts, insurance claims from 9/11 will total about \$50 billion. The Joint Economic Committee recently reported:

The economic losses from the terrorist attacks of September 11th were unprecedented. Estimates of the insured losses from the attacks range from \$30 billion to \$70 billion, with many analysts predicting the final amount to total around \$40 billion to \$50 billion.

– *Economic Perspectives on Terrorism Insurance* – May 2002

The reinsurance industry – those groups that provide insurance to the insurers – is estimated to have shouldered about half the losses from 9/11 and has reportedly pulled back from covering terrorist attacks in the future. Advocates for the bill argue that, absent an active reinsurance market, domestic insurance companies do not have the resources to sustain another attack the size of 9/11, and that a federal backstop was necessary.

The House acted quickly, passing H.R. 3210 on November 29, 2001. This legislation would have the federal government pay 90 percent of any losses from a terrorist attack that exceed \$100 million. Any taxpayer contributions to losses would be recaptured through a general assessment leveled against insurers. The House bill also includes numerous liability reforms including banning punitive damages, limiting non-economic damages, and capping lawyer fees. Finally, the House bill provides for federal jurisdiction over cases resulting from a terrorist attack and allows for consolidation of related cases in the same federal court.

In the Senate, an effort also was made to quickly provide a federal backstop. Senators Dodd, Sarbanes, Gramm, and Enzi came together to support legislation that would cover 90 percent of losses above a \$10 billion threshold. Unlike the House bill, there would be no recapture of taxpayer losses. Like the House bill, the bipartisan Senate approach included liability reforms, including consolidation of cases in federal courts and a ban on punitive damages.

The bipartisan Senate bill was killed when Majority Leader Thomas Daschle objected to the liability provisions. As *CongressDaily* reported at the time:

Senate negotiations on terrorism insurance remained bogged down Tuesday [November 27]. . . . “Consensus” legislation was effectively scrapped after Senate Majority Leader Daschle and other Democrats raised a red flag on the bill’s language limiting punitive damages Dodd . . . indicated that Democrats were regrouping. “We’re meeting with [interest] groups, to see if we can get a Democratic bill,”. . . . Sarbanes said negotiations were continuing, and acknowledged that Daschle was trying to broker a deal “on this side of the aisle.”

– *CongressDaily*, November 28, 2001

Since that time, Senate action on terrorism insurance has been held hostage to a debate over liability reform. Senator Daschle and other Democrats have insisted that the base legislation not protect the victims of terrorist attacks from being assessed punitive damages. For example, on April 25, 2002, Senator Reid requested unanimous consent that the Senate take up the House terrorism insurance bill, but immediately substitute the Dodd-Sarbanes-Schumer substitute as the original text. Republicans have offered competing UC agreements using either the House-passed bill or the original bipartisan legislation as the base text. All of these requests have been objected to.

HIGHLIGHTS

Liability Reform: By all accounts, the inability of both sides to agree on liability provisions related to future terrorist attacks has prevented the Senate from taking up terrorism insurance legislation. Both the House-passed bill and the bipartisan bill effectively vetoed by Senator Daschle include provisions to ban punitive damages and to create a federal cause of action. Existing federal law provides for similar protections to the taxpayer. The Federal Tort Claims Act (28 U.S.C. 2671 *et seq.*) includes a ban on punitive damages, federal jurisdiction, and caps on attorney’s fees.

While the Dodd bill does include federal jurisdiction and protects the federal government from punitive damages, it fails to address the unpalatable circumstance where the owner of a business who is the victim of a terrorist attack is liable for damages, including punitive damages.

Federal Coverage: The Senate bill includes a \$10 billion deductible for all losses from terrorist attacks in 2002. The deductible works like this: Once the Secretary of Treasury determines that all losses sustained from terrorist attacks this year exceed \$10 billion (God forbid), the Treasury will (a) notify Congress and (b) determine what percentage of those losses will be shouldered by taxpayers. If total losses are \$20 billion, then the Treasury will pay 45 percent of any losses suffered by insurers (\$20 billion minus the \$10 billion deductible multiplied by 90 percent).

While attention has focused on the universal deductible of \$10 billion, taxpayers are actually liable for losses of much less. The bill includes a per-company cap that limits losses to individual insurance companies, even if total losses from terrorist attacks this year do not exceed \$10 billion. This cap is equal to \$10 billion times the insurer's share of the domestic property and casualty market. As a result of this provision, a terrorist attack that results in \$10 billion in damages spread among a number of insurance companies could result in taxpayer liability of 60 percent of those losses, or \$6 billion.

Existing Policies: Another concern raised by S. 2600 are those policies which have been sold since 9/11. The Democrat bill includes a provision to provide taxpayer-funded insurance for all policies covering acts of terrorism. The bill does not, however, include any provision for equalizing the premiums between policies sold before and after its enactment. Nor does it address the issue of insurance companies collecting premiums for risks shouldered by the taxpayer.

Presumably, terrorist policies sold following enactment of a federal backstop will be less expensive than those sold prior to the bill's enactment. Otherwise, there's little point in passing this legislation. Yet, while the House bill includes a recapture provision that reduces the implied federal subsidy of existing terrorism insurance policies, the Democrat approach does nothing to address this concern.

BILL PROVISIONS

S. 2600, introduced last week by Senator Dodd and directly placed on the Senate Calendar under Rule 14, is an evolution of the original bipartisan bill negotiated by senators Dodd, Sarbanes, Gramm, and Enzi, absent the liability protection objected to by Senator Daschle. The bill includes the following provisions:

Terrorist Acts: S. 2600 provides that federal reinsurance will apply if the Secretary of Treasury, in concurrence with the Secretary of State and the U.S. Attorney General, certifies that an act of terrorism has taken place. The bill defines an act of terrorism as an attack that:

- Results in losses of at least \$5 million;
- Threatens human life, property, or infrastructure;
- Occurs within the United States or on a domestic airline; and
- Was committed by persons acting on behalf of a foreign interest.

Federal Coverage: Once a terrorist attack has been certified, the federal government would cover the following amounts in 2002:

- 80 percent of annual losses exceeding the per company cap (see below);
- 90 percent of annual losses above the universal \$10 billion cap; and

- 0 percent of annual losses above \$100 billion.

Under the bill, this federal coverage could be extended through 2003 if the Secretary of Treasury determines it is necessary.

Per-Company Cap: The bill covers 80 percent of annual losses exceeding the per company cap. The per-company cap is equal to \$10 billion times the market share of the insurance company involved. For example, AIG – the largest property and casualty insurer in the United States and the world’s largest corporation – has about a 7 percent share of the domestic property and casualty market. Its per-company cap for 2002 would equal \$700 million (7 percent times \$10 billion). Eighty percent of any losses to AIG between \$700 million and \$10 billion would be paid by taxpayers.

Liability Provisions: S. 2600 creates a new, explicit obligation for federal taxpayers. As such, it includes provisions to govern the liability of future terrorist attacks to both taxpayers and private parties. The bill includes the following liability provisions:

Federal Cause of Action: The bill gives federal courts sole jurisdiction over cases arising from a terrorist attack.

Punitive Damages: The law protects taxpayers from paying punitive damages awarded in regard to a terrorist attack. The bill does *not* protect private parties, including those who are themselves the victims of terrorism, from punitive damages. (See “Highlights,” p. 3.)

The bill makes clear that it does not limit any claims made against the actual terrorists.

In-Force Reinsurance Agreements: The bill provides that private reinsurers of insurance policies written prior to the bill’s enactment will be eligible for the same taxpayer-funded coverage as the primary insurance carrier.

ADMINISTRATION POSITION

At press time, the Administration had not released a Statement of Administration Policy on any of the Senate bills. On November 28, 2001, the Office of Management and Budget released a policy statement on the House bill, H.R. 3210. Below is the text of the Statement of Administration Policy on H.R. 3210:

The Administration urges prompt House passage of H.R. 3210 as a step toward enactment of legislation to ensure the continued availability of insurance for terrorist-related acts while encouraging the private sector to build new capacity. In addition, the Administration applauds the House for including reasonable, short-term procedures for terrorist-related litigation.

Procedures for consolidation and management of mass tort litigation arising out of a terrorism incident are a necessary part of any meaningful terrorism insurance proposal, and thus a necessary condition for Administration support of any terrorism insurance bill. However, the Administration has reservations about several key provisions of H.R. 3210. In particular, the Administration is concerned that the assessment mechanism could negatively affect important sectors of the economy. The Administration is also concerned with the administrative complexity of the bill as a whole. The Administration looks forward to continuing to work with Congress to address these and other concerns.

On June 10, 2002, Treasury Secretary Paul O'Neill, National Economic Council Director Lawrence Lindsey, OMB Director Mitchell Daniels, and Council of Economic Advisors Director R. Glenn Hubbard sent a letter to Republican Leader Lott, expressing their support for federal terrorism reinsurance as well as their concerns with the Dodd legislation. The letter included the following:

Last November 1, the Administration publicly agreed to bipartisan legislation negotiated with Chairman Sarbanes, Chairman Dodd, Senator Gramm and Senator Enzi. While the House of Representatives quickly responded to this urgent need by passing appropriate legislation, the Senate did not act and has not passed any form of terrorism legislation in the intervening seven months. . . .

One important issue for the availability of terrorism insurance is the risk of unfair or excessive litigation against American companies following an attack. Many for-profit and charitable entities have been unable to obtain affordable and adequate insurance, in part because of the risk that they will be unfairly sued for the acts of international terrorists.

To address this risk at least two important provisions are essential. First, provisions for an exclusive federal cause of action and consolidation of all cases arising out of terrorist attacks, like those included in the Air Transportation Safety and System Stabilization Act, are necessary to provide for reasonable and expeditious litigation.

Second, the victims of terrorism should not have to pay punitive damages. Punitive damages are designed to punish criminal or near-criminal wrongdoing. Of course such sanctions are appropriate for terrorists. But American companies that are attacked by terrorists should not be subject to predatory lawsuits. The availability of punitive damages in terrorism cases would result in inequitable relief for injured parties, threaten bankruptcies for American companies and a loss of jobs for American workers. . . .

The bipartisan public agreement reached between the Administration and Chairman Sarbanes, Chairman Dodd, Senator Gramm and Senator Enzi last fall provided these minimum safeguards. **We would recommend that the President not sign any legislation that leaves the American economy and victims of terrorist acts subject to predatory lawsuits and punitive damages.**

COST

There is no cost estimate for S. 2600. The bill makes the taxpayer liable for losses resulting from future terrorist attacks above certain limits.

POSSIBLE AMENDMENTS

McConnell/Gramm:

Amendment reflects the original agreement among the Administration, Senators Gramm and Enzi, and Democrat Senators Sarbanes and Dodd, including a \$10 billion deductible, a ban on punitive damages for all parties, and federal jurisdiction of claims. In a compromise, the McConnell amendment allows punitive damages to be assessed against private parties if they have been convicted of a felony in relation to the terrorist attack.

Nelson (FL): Amendment to prohibit redlining and to cap premiums for insurance policies covering terrorist attacks.

Stevens: To federal insurance backstop for “Acts of God.”

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